IN THE HIGH COURT OF GUJARAT AT AHMEDABAD

CHARTER ACCOUNTANT REFERENCE No 1 of 2004

For Approval and Signature:

HON'BLE MR.JUSTICE D.A.MEHTA
and
HON'BLE MS.JUSTICE H.N.DEVANI

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1. Whether Reporters of Local Papers may be allowed to see the judgements? : NO

2. To be referred to the Reporter or not? : YES

3. Whether Their Lordships wish to see the fair copy of the judgement? : NO

4. Whether this case involves a substantial question of law as to the interpretation of the Constitution of India, 1950 of any Order made thereunder? : NO

5. Whether it is to be circulated to the concerned Magistrate/Magistrates,Judge/Judges,Tribunal/Tribunals? : NO

COUNCIL OF THE INSTITUTE OF CHARTERED ACCOUNTANTS OF INDIA

Versus

MILIND KANTILAL SHAH, CHARTERED ACCOUNTANT

Appearance:

1. CHARTER ACCOUNTANT REFERENCE No. 1 of 2004
MR SN SOPARKAR, SR. ADVOCATE WITH MRS SWATI SOPARKAR for the Petitioner
MR AK CLERK for Respondent

CORAM : HON'BLE MR.JUSTICE D.A.MEHTA
and
HON'BLE MS.JUSTICE H.N.DEVANI

Date of decision: ___/__/2005

CAV JUDGEMENT

(Per : HON'BLE MS.JUSTICE H.N.DEVANI for the Court)

1. This reference is made under Section 21(5) of the Chartered Accountants Act, 1949 (the Act), by which the Council of the Institute of Chartered Accountants of India (the Council), who has forwarded the case to this Court after finding the respondent, a Member of the Institute of Chartered Accountants of India, guilty of professional misconduct within the meaning of Clauses (5), (6) and (7) of Part I of the Act read with Sections 21 and 22 of the said Act.

2. The matter arises out of a complaint filed by Shri R. Banerjee, Managing Director of the Gujarat State Financial Corporation (GSFC) against the respondent - Shri Milind Kantilal Shah, who is a practising Chartered Accountant and who had issued a certificate which the complainant - Corporation relied upon in order to disburse the loan to a Company named M/s Maimoon Textiles Pvt. Ltd. The complainant made the following allegations against the respondent :

"1.1 Based on the certificate dated 26-09-1994 of the Respondent, the Complainant Corporation worked out the amount of eligible disbursement of Rs.11,25,000/- for M/s Maimoon Textiles (P) Ltd., Surat. The certificate submitted by the Respondent is false because as per the inspection conducted by the staff members of the Complainant Corporation, the aforesaid unit had not constructed the factory and the land was an agricultural land. As per the Respondent's certificate, the unit incurred an expenditure of Rs.5.73 lacs on the construction of factory building. As there was no factory building, there was no machinery on the site; whereas, as per the Respondent's certificate, the unit had purchased machineries and accessories of Rs.16.53 lacs and the same were brought on site. Also, the Respondent had mentioned in the certificate that the certificate was issued after personally verifying the assets of the unit. On the other hand, as per the inspection carried

out by the officers of the complainant Corporation, the assets were not in existence.

1.2 Therefore, as per the complaint, the Respondent is guilty of professional misconduct falling under Classes (5), (6) and (7) of Part I of the Second Schedule to the Chartered Accountants Act, 1949."

2.1 A copy of the said compliant was sent to the respondent vide the Institute's letter dated 16th August, 1996 with a request to send his written statement to the Institute. The respondent submitted his written statement on 25th September 1996. The complainant submitted his rejoinder on 29th October, 1996. The respondent submitted his comments on 11th February, 1997. In accordance with the provisions contained in Regulation 12(11) of the Chartered Accountants Regulations, the aforesaid papers containing the complaint, the written statement, the rejoinder and the comments were considered by the Council at its meeting held in April 1997 at New Delhi. The Council was prima facie of the opinion that the respondent was guilty of professional and / or other misconduct and accordingly, referred the case to the Disciplinary Committee constituted under the Act, for inquiry.

2.2 On perusal of the documents on record and after recording the submissions of the complainant and the respondent, and after examination of the witnesses, the Committee submitted its report dated 11th December, 2001. The Committee came to the conclusion that the respondent was guilty of professional misconduct within the meaning of Clauses (5), (6) and (7) of Part I of the Second Schedule to the Act read with Sections 21 and 22 of the Act.

2.3 A copy of the report of the Disciplinary Committee was forwarded to both the parties vide the Institute's letter dated 30th July, 2002 and they were informed that the said report would be considered by the Council at one of its forthcoming meetings. The parties were requested to send their written representations, if any, in the matter and were informed that if they so desire, they may appear before the Council either in person or through a Member of the Institute, duly authorized by them and make their submissions.

2.4 The report of the Disciplinary Committee was

placed before the Council which consisted of 17 members (including the members of the Committee), and was taken up for consideration in its 230th Meeting held on 26th and 28th December, 2002. On consideration of the report of the Disciplinary Committee along with the written representations received from the Complainant Corporation dated 27th August, 2002 and 4th October, 2002 and written representations received from the respondent dated 10th October, 2002, 16th October, 2002, 31st October, 2002 and 19th December 2002, the Council decided to accept the report of the Disciplinary Committee, and accordingly found the respondent guilty of professional misconduct within the meaning of Clauses (5), (6) and (7) of Part I of the Second Schedule to the Act read with Sections 21 and 22 of the Act. The Council also decided to recommend to the High Court that the name of the respondent be removed from the Register of Members for a period of one year.

2.5 The disciplinary case was forwarded by the Council to this Court in terms of Section 21(5) of the Act.

3. Mr.S.N.Soparkar, learned Senior Advocate appearing for the Institute, contended that the Council had found the respondent guilty of professional misconduct within the meaning of Clauses (5), (6) and (7) of Part I of the Second Schedule to the Act read with Sections 21 and 22 of the Act on the basis of the material on record gathered during the inquiry conducted by the Disciplinary Committee, which has been statutorily constituted. It was submitted that the recommendation of the Council be accepted and the name of the respondent be removed from the Register of Members for a period of one year.

3.1 The learned Senior Advocate invited the attention of the Court to the evidence of the witnesses, namely, Shri Tahir Ali Vasi, a director of M/s Maimoon Textiles Pvt. Ltd., Shri A.H.Nasir, Shri Sirajuddin Khasi, an Advocate and Notary, Shri Ishwarbhai Patel, the Sarpanch of Masma village, Shri Vasi, a Director of M/s Maimoon Textiles Pvt. Ltd., Shri R.L.Patil, an engineer of the GSFC, Shri Buch, an employee of the GSFC, Shri R.T.Jadav, Senior Inspector with the GSFC and the respondent Shri Milind Shah. The learned Senior Advocate submitted that, from the evidence of the witnesses, it appears that one Shri Hanif Memon had an important role to play in the matter. However, for reasons best known to the respondent, he had chosen not to examine Shri Hanif Memon. Had Shri Hanif Memon been examined, all facts,

which would ultimately give a complete scenario, would have come on the record.

3.2 The learned Senior Advocate submitted that GSFC disburses funds on the strength of the certificate issued by the Chartered Accountant. That GSFC had not carried out any inspection, as it had relied upon the certificate of the Chartered Accountant. The attention of the Court was invited to the certificate issued by the respondent and it was submitted that the discrepancy as to capital was indefensible. It was contended that if the respondent had verified Form No.2, he could have easily found the amount of share capital raised by the Company. It was pointed out that, when admittedly the capital was of Rs.4,000/-, the respondent had given the certificate for Rs.5 lakhs. It was contended that the basic document which the respondent was supposed to verify for the purpose of deciding how much share capital the company has raised, was Form No.2; however, as stated by the respondent in his deposition, he had not verified Form No.2. It was submitted that the respondent has acted with sheer callousness.

3.3 The learned Senior Advocate submitted that if the certificate is to be accepted at face value, the person who issues it must do so with due care and caution. If he does not do so, the credibility of the certificate is affected. It was submitted that even though the respondent may not be involved in the fraud, he has permitted the fraud to be perpetuated. It was argued that, as regards the share capital, incorporation and bank transactions, the respondent has no answer, so his say that he was shown some some other place is belied. It was argued that the respondent had not even bothered to verify the books of account prior to issuance of the certificate. Referring to the Memorandum of Association of the Company, the learned Senior Advocate pointed out that the Company was incorporated on 13-5-1993. The learned Senior Advocate referred to the deposition of the respondent wherein he had stated that when he had verified the books of account, he saw that the major part of the expenditure was incurred from 1-1-1993. It was contended that the respondent could not have verified the books of account as the Company was not incorporated on that date. It was submitted that this was not a case of mere carelessness, but was a case of gross negligence.

3.4 The decision in case of Council of Institute of Chartered Accountants of India v. P.C.Parekh, reported in (2003) 129 Taxman 80 (Gujarat) was cited to point out that a large section of public relies on the objectivity

and integrity of professional accountants to maintain the orderly functioning of commerce. The Members of the Institute are bound to act in a manner consistent with the good reputation of the profession and that, they should refrain from any conduct which might bring discredit to the Institute. If the professional bodies do not take strong steps to not only policing their members but also to ensure that the public believes that they are doing so, it would call for increasing governmental policing.

3.5 It was submitted that such great credibility was attached to a certificate bearing the signature of a Chartered Accountant that it was the basis of issuance of funds by GSFC. It was submitted that if the Institute does not take action it diminishes the credibility of the members of the Institute. It was contended that the very purpose of obtaining a certificate is frustrated if the certificate cannot be relied upon. It was submitted that the respondent ought to have known that the certificate issued by him was false and that it was a fact that he had reason to believe that it was false but did not make necessary inquiry.

3.6 The learned Senior Advocate referred to the written statement of the respondent wherein, in defence, the respondent had denied that the unit was disbursed money on the basis of his certificate only, since it was the procedure of the GSFC to obtain legal clearance of their own full fledged Legal Department armed with experts in the legal field and only thereafter, the money was released. It was submitted that the petitioner Institute is not concerned with as to whether GSFC is at fault, but the Institute is primarily concerned with the conduct of its own members.

3.7 The decision in the case of Council of Institute of Chartered Accountants v. M.R.Shah, reported in (2004)2 GLH 610 was cited wherein this Court, after referring to the Scheme of the Act as well as the provisions of the Income Tax Act, 1961, observed that the said provisions are indicative of the extent that a Chartered Accountant is looked upon by the society, with special reference to the corporate world, as being competent to discharge various statutory duties and responsibilities as a qualified professional. The Court observed that the said position of law clearly demonstrates the faith that various Government Departments have in the professional qualifications, competency and integrity of a Chartered Accountant and hence, the various statutory duties and responsibilities

cast upon a Chartered Accountant under various provisions of the Act. It was stated that there are other statutes like Co-operative Societies Act, Bombay Public Trusts Act etc. where also, the importance of the report of the Chartered Accountants has been statutorily recognized and accepted. The Court observed that it is, in the aforesaid context, that the conduct of the respondent has to be tested and appreciated in the light of the evidence placed on record.

3.8 The decision of the Hon'ble Supreme Court in the case of In re "P" An Advocate, reported in AIR 1963 SC 1313, was cited for bringing out the distinction between "negligence" and "gross negligence". It was held that mere negligence or error of judgement on the part of the Advocate would not amount to professional misconduct. It was observed that error of judgement cannot be completely eliminated in all human affairs and mere negligence may not necessarily show that the Advocate who was guilty of it can be charged with misconduct. It was held that different considerations arise where the negligence of the Advocate is gross. It may be that before condemning an Advocate for misconduct, courts are inclined to examine the question as to whether such gross negligence involves moral turpitude or delinquency. In dealing with this aspect of the matter, however, it is of utmost importance to remember that the expression "moral turpitude or delinquency" is not to receive a narrow construction. It was held that, wherever conduct proved against an Advocate is contrary to honesty, or opposed to good morals, or is unethical, it may be safely held that it involves moral turpitude. A wilful and callous disregard for the interests of the client may, in a proper case, be characterized as conduct unbefitting an Advocate. It was observed that in dealing with matters of professional propriety, one cannot ignore the fact that the profession of law is an honourable profession and it occupies a place of pride in the liberal professions of the country. Any conduct which makes a person unworthy to belong to the noble fraternity of lawyers or makes an advocate unfit to be entrusted with the responsible task of looking after the interests of the litigant, must be regarded as conduct involving moral turpitude.

3.9 It was submitted that, similarly, any conduct of the Chartered Accountant, which makes him unworthy of belonging to the noble fraternity of Chartered Accountants or makes him unfit to be entrusted with the various statutory duties cast upon him, must be regarded as conduct involving moral turpitude.

3.10 The learned Senior Advocate submitted that, in the facts of the present case, the respondent did not exercise due care and caution and had displayed a callous attitude towards his duties. It was urged that the certificate issued by the Chartered Accountant was recognized as a final word by the business world, hence, such conduct cannot be countenanced. It was submitted that, in taking an overall view of the facts of the case, the recommendation of the Council was required to be accepted and the name of the respondent was required to be removed from the Register of Members for a period of one year.

4. Mr.A.K.Clerk, the learned Counsel appearing for the respondent, referred to the written representation made by the respondent on the report of the Disciplinary Committee, wherein it is stated that the Disciplinary Committee has failed to appreciate the true facts and sequence of events. It was the respondent's case that the loanee had shown him premises at the site, but later on, it turned out to be some other premises. It was submitted that the Disciplinary Committee has not accepted the version and submission of the respondent on the ground that there was absence of any record, noting or other evidence which the respondent, according to the Disciplinary Committee, should have kept in his possession. It was contended that the Disciplinary Committee failed to appreciate that, in the circumstances of the case, there was no reason for the respondent to keep any record, noting or other evidence and that the Disciplinary Committee was wrong in holding that the respondent "should have kept in his possession" these records, noting or other evidence. It was submitted that the respondent took inspection of the factory premises in about August / September 1994. At that time, the respondent had all his records, notings etc. The respondent was taken by the loanee for a site visit to the factory in about the month of August 1994. The respondent was taken to a vast piece of land at Vadod Patiya, Village Masma, Taluka Olpad, Dist. Surat. The respondent found that there was a factory building and there were machineries also in the said factory building. That, he also saw some persons in the said factory building, and that he was introduced to some of them as Technicians of the loanee. The loanee also produced before the respondent various vouchers, receipts etc. It was submitted that it was only somewhere in February 1995 that officers of the complainant Corporation informed the respondent that there was something suspicious about the loanee; that the loanee appeared to be not having any

land or factory, nor the loanee appeared to have purchased any machinery. It was submitted that the respondent immediately contacted the loanee and the loanee ultimately paid the entire dues of the Corporation by March 1995, and informed the respondent that the dispute with the Corporation was settled. It was submitted that even the officers of the complainant Corporation appreciated the respondent's efforts and thanked the respondent for getting the full repayment of the dues from the loanee. It was contended that the respondent was not aware that the complaint was filed on 3-4-1996, more than a year after the Corporation was fully paid its dues. The respondent came to know about the complaint having been filed only when he received the notice about the complaint in about the month of August 1996, i.e. about 17 months after the Corporation was fully repaid its dues in March 1995. It was submitted that since the dues of the complainant - Corporation were already paid up, and since the respondent was informed and even thanked by the officers of the complainant Corporation, that their dues were fully paid by the loanee, the respondent considered the matter to have come to an end and there was no reason for the respondent to keep any record, noting etc. about the matter.

4.1 The learned Counsel referred to page No.22 of the enclosure of the Complainant Corporation's disbursement note that all legal formalities were completed, and submitted that the sanction was earlier in point of time and that the respondent was in the picture only at the stage of disbursement.

4.2 The learned Counsel submitted that the intention behind GSFC filing the complaint did not appear to be bonafide. He submitted that no action had been taken against the officials of the GSFC. No criminal complaint had been filed and that, except for the present complaint, no other proceedings have been undertaken. It was submitted that the conduct of the parties also ought to be taken into consideration. The respondent, when he was approached in 1995, did not shirk from his responsibility to see to it that the amount due was repaid. It was contended that GSFC, on the other hand, having collected the money, after a year, filed a complaint wherein there is not a whisper about the money being returned back; on the contrary, it is the say of the Corporation that it has suffered a loss. It was submitted that GSFC conveniently omitted the fact that the loan was disbursed after completion of legal formalities. It was contended that GSFC is also equally at fault and that the loan is not disbursed only on the

strength of the certificate issued by the respondent. It was submitted that, despite the fact that the money had been repaid, GSFC had suppressed the said fact from the Council. It was submitted that when the complaint is of such a serious nature, it was incumbent upon the Corporation to come forth with the correct facts. The learned Counsel referred to the complaint filed by GSFC and submitted that no explanation had come forth for the delay in filing the said complaint.

4.3 The learned Counsel submitted that various factors are required to be kept in mind prior to taking any action against the respondent. Firstly, the past record of the practice of the respondent is required to be considered. That the respondent had sixteen years of practice and there was no prior complaint. Secondly, the respondent had been dealing with such matters in more than a hundred projects, yet there was no complaint except the present one. Thirdly, as soon as it was brought to the notice of the respondent, he immediately took steps to see that the money is repaid. It was submitted that this conduct of the respondent shows his character, that he is concerned that no loss should be suffered by the Corporation, and that, his own reputation is not sullied. It was submitted that the respondent was not a crook and not the type who would take some illegal benefit. It was contended that the principal allegation against the respondent was that he was negligent in issuing the certificate.

4.4 The learned Counsel submitted that a professional body like the Council is in the position of loco parentis so far as its members are concerned and that the possibility of the respondent actually having been misled cannot be ignored. It was contended that the respondent's entire career should have been taken into account. It was submitted that his owning up to the responsibility shows his conduct. Referring to the written submissions dated 10th October, 2002 submitted by the respondent to the Council, the learned Counsel pointed out that, between 31st January, 1994 and 26th September, 1994, GSFC had shown that an amount of Rs.5 lakhs were given as advance, and submitted that may be formalities were not completed, so it may not have been shown in the balance sheet. It was contended that when GSFC note shows an advance of Rs.5 lakhs, there was no reason for the Chartered Accountant to disbelieve it. It was contended that GSFC has very conveniently forgotten that it has also undertaken the legal formalities.

5. During the course of inquiry, the Disciplinary

Committee had recorded the evidence of various witnesses. Shri Tahir Ali Vasi, a Director of M/s Maimoon Textiles Pvt. Ltd. had stated that the Company was established in 1993 for the purpose of setting up a textile manufacturing unit, and that the land had been purchased at Masma, near Surat, for the said purpose. That thereafter, a loan was applied for from GSFC for the purpose of setting up the project. However, by the time the formalities of purchase of land and sanction of loan could be completed, the entire industry was in a recessionary phase. Ultimately, they decided that it would not be worthwhile in proceeding with the project. At that point of time, Shri Hanif Memon came into the picture with an offer by which the investors would be able to recover the amount invested by them by selling off the project to some other party. That, in this context, he was asked to furnish the papers to a Chartered Accountant named by Shri Hanif Memon. The Chartered Accountant was Shri Milind K. Shah, the present respondent. The said witness also stated that, at no point of time during his tenure or to his knowledge even thereafter, had he any knowledge of any construction of plant or building being done at the premises. He was also not aware of any books being produced before the respondent for purpose of verification or certification. The only reason why they had gone to the respondent was because of the suggestion of Shri Hanif Memon, and it was he who advised that the directors should be changed. He also claimed that he and / or other directors had never approached the respondent for the impugned certificate and that all these acts had been done by Shri Hanif Memon.

5.1 Upon examination of witness Shri A.H.Nasir, the Committee came to the conclusion that the original directors acted as conduits for the company to be passed on to a new set of Directors and despite money having been received in the name of the company, the same was probably received by certain persons other than the original director. When inquiry was commenced by GSFC, the persons who had actually received the money arranged to pay it back.

5.2 Shri Ishwarbhai Patel, the Sarpanch of Masma village, stated that no permission for structure of the sort that is claimed to exist has ever been granted nor is there any such unauthorized structure in the said area which falls within the village boundaries. He further confirmed that there was no factory of the said M/s Maimoon Textiles Pvt. Ltd. in Masma village, and hence, any person claiming that there was such a structure, was

not correct in such statement.

5.3 Shri R.L.Patil, an Engineer employed by GSFC, stated that he had gone to find out the factual position in regard to Maimoon Textiles Pvt. Ltd. Upon reaching the site, on inspection, he could not verify any assets because there was no structure at the site and no fixed asset at the site, or at least at the site which was indicated to him as plot Nos. 13 and 14.

5.4 Witness Shri Buch, employed with GSFC, spelt out the policy of the Corporation in regard to disbursal of such loans. He stated that, at the relevant time, it was the policy to permit disbursal upto 50% of the loan sanctioned upon receipt of the Chartered Accountant's certificate confirming that the necessary expenditure had been incurred and the building construction and machinery were available and verified on site. It was submitted that this was particularly because of the positive assertion contained at the end of the certificate which states that the Chartered Accountant has "read the guidelines for issue of certificate by M/s Gujarat State Financial Corporation Ltd. and I have certified the above particulars in accordance therewith. Physical existence of the assets has been personally verified by me by carrying out inspection as well as verifying the vouchers, evidencing the payment made to the parties." Based on this positive assertion, in order to facilitate the borrower to proceed with the project speedily, no further verification is insisted at that stage.

5.5 Shri R.T.Jadav, Senior Inspector with GSFC, testified in respect of the inspection carried out by him in January 1996. He stated that, at that time, he did not find any construction on the plot purportedly belonging to the borrower. As per his report, the people in the local area were not aware of any such company as M/s Maimoon Textiles Pvt. Ltd. The report submitted by him confirmed that there was cultivation of paddy and wheat on the said plots and certain other units were functioning nearby.

5.6 Upon being examined by the Committee, the respondent Shri Milind K. Shah had stated that he had been introduced to M/s Maimoon Textiles Pvt. Ltd. and to Shri A.H.Nasir by one of his friends, Shri Hanif Memon. The respondent confirmed that although he had not earlier been associated with the Company, he found nothing wrong in assisting the Company, with regard to procuring of loan from the Gujarat State Financial Corporation Ltd. In fact, he did not enquire about the

auditor of the Company or about the audit itself and he did not consider it relevant for the purpose of certification.

5.7 The respondent had asserted that he had actually visited the site of the factory before issuance of the impugned certificate. It was stated by the respondent that he had gone by a car to Masma and when he visited the site, he had seen that there was a board indicating that this was the site of M/s Maimoon Textiles Pvt. Ltd. It was stated that the building which he had certified was under construction in September 1994, and that part of the machinery was also available at the site. The respondent confirmed that he had made notes with regard to the said verification and had issued a certificate after going through the necessary invoices which had been forwarded to his office. He thus confirmed that it was on the basis of the noting made at the time of the visit to the factory and the further co-relation of other invoices and documents produced for verification that he had issued the necessary certificate. It was the say of the respondent that he had thus complied with the condition of personal physical verification that was stated in the GSFC certificate. On being asked by the Committee to produce the notings made at the time of physical inspection, the respondent, however, stated that the said notes and records are not presently available with him. Upon inquiry as to when he became aware that there were certain problems / queries in regard to the certificate issued by him, the respondent stated that he became aware of this situation in February 1995. Upon inquiry as to why he did not have the record of verification carried out, especially the working notes, since he became aware of some difficulties, he stated that he had not felt it important to retain the said papers. On being questioned with regard to whether he had matched the machine numbers mentioned in the invoices verified by him with the machine numbers on the actual machines, the respondent had stated that no machine numbers were mentioned on the machinery.

5.8 During the course of examination by the Committee, the respondent confirmed that the expenses covered in the certificate dated 26th September, 1994 were incurred from the period commencing from 1st January, 1993. When it was pointed out to him that the company had been incorporated only in May 1993, the respondent was unable to give a suitable explanation in that regard. The Committee found that the respondent had made no inquiry as to who were the first auditors of the company and what was the state of the balance sheet of

the said company. On being pointed out that, at page No.3 of his certificate, he had stated that the share capital of the Company was Rs.5,10,000/- and whether the same had been properly verified by him, he was once again unable to satisfactorily explain the same. The attention of the respondent was drawn to the aggregate amount of unpaid suppliers which indicated that the suppliers were unpaid to the extent of Rs.11.34 lakhs and as to how they had agreed to extend so much credit, he was once again at a loss to give a logical explanation.

6. Upon consideration of the evidence on record and the statements of the complainant and the respondent, the Disciplinary Committee was of the view that the respondent had not taken due care in carrying out the verification required before making the assertion contained in paragraph 10 of the impugned certificate, namely, that the respondent had verified the particulars stated therein after carrying out the physical verification as regards the existence of the assets, verification of vouchers etc., personally.

6.1 The Disciplinary Committee also found that the respondent had not verified the Memorandum and Articles of Association of the Company, nor had he verified Form No.2, required to be filed as per the Companies Act, in regard to allotment of equity capital. It was noted that the audited balance sheet of the Company was signed by Shri S.S.Karanchiwala as at 31st March, 1994. The balance sheet signed by the auditor bore the date of 25th June, 1994 and should, therefore, have been available to the respondent on the date of issuance of the certificate i.e. 26th September, 1994. The said balance sheet showed a share capital of Rs.4,000/- only and the gross block of fixed assets was reflected at Rs.39,000/- only. The figures in the balance sheet and in the certificate issued by the respondent were grossly at variance with each other, and hence, the Disciplinary Committee found that it was difficult to accept that the respondent, while issuing the impugned certificate, had taken this aspect into consideration. In fact, the respondent had stated on record that he had neither inquired as to who the auditor was, nor had he sought to co-relate the data with the audited balance sheet.

6.2 The Disciplinary Committee was of the opinion that, in the absence of any record, noting or other evidence which the respondent should have kept in his possession and should have produced before the Disciplinary Committee, the plea that the respondent may have been taken to some other premises and had been shown

a building which is stated to have been constructed at the said site could not be accepted. The Disciplinary Committee also found that the certificate in question was dated 26th September, 1994 and the fact that there was something irregular in regard to the said transaction was apparent in February 1995 itself, if not earlier, and therefore, the plea that the respondent had not retained the record of the said verification was not found acceptable. The Disciplinary Committee was of the opinion that the intervening period was not long enough to justify the destruction of working notes which the Chartered Accountant would normally be expected to maintain in regard to the certification carried out by him. The Committee found that the admitted failure to verify certain other circumstances and evidences which would have a direct bearing on the figures certified by the respondent also indicates that the respondent was guilty of being grossly negligent in the conduct of his duties as a practising Chartered Accountant and had thereby committed professional misconduct within the meaning of Clause (7) of Part I of the Second Schedule to the Act.

6.3 The Disciplinary Committee was of the opinion that the respondent knew or should have known that the expenditure purported to have been incurred in regard to the construction of the building and for purchase of machinery could not have been incurred in absence of availability of adequate funds. The Disciplinary Committee observed that no evidence of the money having been brought into the account of the Company through the Company's bank account had been produced at any stage which the respondent should have known or having known had failed to disclose the same. The Disciplinary Committee found that the respondent had failed to disclose the fact that there was in fact no inflow of funds as share capital, no return of allotment, no verification of bank account, no cross tallying with the balance sheet and was, therefore, guilty of not disclosing material facts known to him which was not disclosed in the financial statement, but disclosure of which was necessary to make the statement not misleading. The Disciplinary Committee was, therefore, of the view that the respondent was guilty of professional misconduct within the meaning of Clause (5) of Part I of the Second Schedule to the Chartered Accountants Act, 1949.

6.4 The Disciplinary Committee also found that the respondent had failed to report a material mis-statement known to him to appear in a financial statement with which he was concerned in his professional capacity, and

was therefore, guilty of professional misconduct within the meaning of Clause (6) of Part I of the Second Schedule to the Chartered Accountants Act, 1949. The Disciplinary Committee accordingly found the respondent guilty of all the charges levelled against him.

7. This Court, in the case of Council of the Institute of Chartered Accountants of India v. P.C.Parekh (supra), has observed that, a hallmark of any noble profession is adherence by its members to a common code of values and conduct established by its administrative body, including maintaining an outlook which is essentially objective and acceptance of a duty to the society as a whole. Acceptance of its responsibility to public is a distinguishing mark of a profession. A large section of public relies on the objectivity and integrity of professional accountants to maintain the orderly functioning of commerce. Such reliance imposes a public interest responsibility on the accounting profession. It was observed that professional accountants have an important role to play in the society. Investors, creditors, employees and other sectors of the business community as well as the Government and the public at large rely on professional accountants for sound financial accounting and reporting effective financial management and competent advice on a variety of business and taxation matters. It was held that, the attitude and behaviour of the professional accountants in providing such services have an impact on the economic well being of the community and the country. The Court observed that, it is in the best interest of the worldwide accountancy profession to make known to the users of the services provided by the professional accountants that they are executed at the highest level of performance and in accordance with the ethical requirements that strive to ensure such performance. This is why the Code of Ethics keeps in mind the public service and user expectations of ethical standards of professional accountants, to keep up to the expected standards. The Court further observed that, thus, the universally recognized objectives of accountancy profession are to work to the highest standards of professionalism, to attain the highest levels of performance and generally to meet the public interest requirement. These objectives require four basic needs to be met, namely, (i) credibility in information and information system, (ii) professionalism, (iii) quality of services and confidence of users of professional service of professional accountants; and (iv) a framework of professional ethics which governs the provision of those services. The Court also held that, in order to

achieve the objectives of the accountancy profession, professional accountants have to observe a number of pre-requisites or fundamental principles, which are, integrity, objectivity, professional competence and due care, respect confidentiality of information, good professional behaviour and observance of high technical professional standards. The Court observed that, a professional accountant should not be associated with any return or communication in which there is a reason to believe that it contains a false or misleading statement, contains statements or information furnished recklessly or without any real knowledge of whether they are true or false, or omits or obscures information required to be submitted and such omission or obscurity would mislead the revenue authorities. The Court observed that these professional standards are imperative and arise from the fundamental principle that a professional accountant should be straight forward and honest in performing professional service. The Court also observed that a professional accountant should not be a party to falsification of any record, or knowingly or recklessly supply any information or make any statement which is misleading, false, or deceptive in any material particular.

7.1 Keeping the aforesaid principles in mind, the conduct of the respondent would have to be tested in the context of the responsibilities of a Chartered Accountant as well as the high standards of objectivity and integrity that he is required to maintain in his professional conduct, considering the impact that the attitude and behaviour of the professional accountants in providing their services have on the economic well-being of the community and the country.

7.2 The complainant, Gujarat State Financial Corporation is engaged in financing Small and Medium Scale Industrial Undertakings. The Corporation has taken certain pragmatic measures to speed up the process of loan disbursal. One of these measures has been that since borrowers require funds up-front at the commencement of a project, a significant responsibility has been cast on the Chartered Accountants whose certificates are accepted for the purpose of initial disbursement. In the facts of the present case, a loan of Rs.22,20,000/- was sanctioned to M/s Maimoon Textiles Pvt. Ltd. on 27-7-1994 to set up their project at Plot No.14-15, Block No.192, Village Masma, Tal. Olpad, Dist. Surat. The loan granted to an industrial unit is to be disbursed on the submission of a Chartered Accountant's certificate as per the prescribed proforma about assets

created by the unit after completion of legal formalities. The loanee produced the certificate dated 26-9-1994 of M/s Milind K. Shah and Co., which was signed by the Proprietor Shri Milind K. Shah, Membership No.36482. On the basis of this certificate, the Corporation worked out the amount of eligible disbursement at Rs.11,25,000/- and the same was accordingly disbursed. Thereafter, as per the procedure followed by the Corporation, the inspection of the unit was carried out by a staff member of the Surat Regional Office of the Corporation on 18th February 1995. In the inspection report, it was stated that the loanee unit has not constructed the factory and the land was an agricultural land. Whereas, as per the certificate submitted by M/s Milind K. Shah & Co., the loanee unit has incurred an expenditure of Rs.5.73 lakhs on the construction of factory building. As there was no factory building, there was no machinery on the site. Whereas, in the certificate of the Chartered Accountant, it is shown that the unit has purchased machineries and accessories of Rs.16.53 lakhs and the same were brought on site. It was also stated in the certificate that the certificate has been issued after personally verifying the assets of the loanee unit. Whereas, in fact, at the time when inspection was carried out by the officers of the Corporation, the assets were not in existence. It was, therefore, the charge of the complainant that the respondent had issued a patently false certificate whereby the respondent should be held guilty of professional misconduct under the Act, as under :

(a) Clause (5) of Part I of the Second Schedule :

failure to disclose a material fact known to him, which is not disclosed in the financial statement, but disclosure of which is necessary to make the statement not misleading.

(b) Clause (6) of Part I of the Second Schedule :

fails to report a material mis-statement known to him to appear in a financial statement with which he is concerned in a professional capacity.

(c) Clause (7) of Part I of the Second Schedule :

is grossly negligent in the conduct of his professional duties."

7.3 The fact that the respondent had issued the certificate in question, is not in dispute. Before the petitioner Council, it was the case of the respondent that it is the procedure of GSFC to obtain a legal clearance of their own full fledged legal Department armed with experts in the legal field and only thereafter, the money was released. The respondent had denied that the unit was disbursed money on the basis of his certificate only. It was the case of the respondent that he was actually taken for site visit to the factory of the company in the month of August 1994. That there was a factory building as well as machineries in the said building, and that, he was introduced to certain technicians and a few days later various vouchers, receipts, statements of accounts etc. indicating the expenditure incurred by the Company for the said project including for the purchase of machineries, etc. was produced before him. That relying upon the said documents and the site visit, the respondent had issued the certificate dated 26-9-1994. It was the case of the respondent that, both he and GSFC had been defrauded by the company and that, upon coming to know that the company did not have the land or the factory nor had they purchased the machinery as made out before him, he inquired into the matter and thought that the best course of action was to pressurize the company to repay the entire outstanding dues of GSFC. That ultimately he succeeded in making the company repay the entire dues of the complainant Corporation. That the officers of the Corporation had appreciated his efforts and thanked him for the full repayment of their dues. It was the case of the respondent that since the money was repaid, there was no financial loss to the Corporation. The respondent submitted that he did not know the material facts as they were fraudulently and illegally concealed from him, and that, therefore, the question of his concealing or not disclosing facts not known to him, did not arise. It was the case of the respondent that he had checked up all necessary and relevant vouchers relating to the transactions that were produced before him by the company, but it had now transpired that the same were fake, fabricated or concocted ones. It was the case of the respondent that, all throughout he did not know various facts. That if the respondent did not know anything (it is a different matter whether "he should have known" or "ought to have known"), there is no question of his being guilty of "not disclosing" information relating to material facts. That, as per

Clause (5) of Part I of the Second Schedule, a person is guilty of professional misconduct if he fails to disclose material facts "known to him" as distinguished from material fact which he ought to have known or which he should have known. That there was no clear finding of the Disciplinary Committee that the respondent knew various material facts. It was the say of the respondent that, therefore, he cannot be held liable under Clause (5) of Part i of the Second Schedule for not disclosing information relating to material facts which he "should have known" or "ought to have known". The respondent had also contended that the Disciplinary Committee had not pointed out which material statement which was known to him that the respondent failed to report.

7.4 As regards the observation of the Disciplinary Committee that the audited balance sheet of the company as on 31-3-1994 which showed the capital of Rs.4,000/and reflected gross block of Rs.39,000/- of fixed asset, it was contended that the Disciplinary Committee ought to have appreciated that the certificate issued by the respondent was dated 26-9-1994 i.e. six months after the audited balance sheet date and that it was a fact that assets were created during the intervening period of six months which was also evident from the appraisal note of GSFC where an amount of Rs.5 lakhs was shown as advance to contractor and machinery suppliers. As regards the capital, as per the certificate having been shown to be Rs.5,10,000/-, it was submitted that the said capital was raised during the intervening period, when the capital was Rs.4,000/- and that, merely lack of ROC formalities would not vitiate the fact that the fund was received towards capital and ROC formalities would be done subsequently. It was also submitted that GSFC had an extensive internal control system whereby the status of the loanee is carefully screened before issuing sanction letter, on which a Chartered Accountant would normally rely; and the loan is disbursed subsequently. Therefore, the blame cannot be attributed solely to the Chartered Accountant because of the certificate issued by him.

8. Upon perusal of the certificate dated 26-9-1994 issued by the respondent, it is seen that the respondent has certified that the company has purchased machineries worth Rs.14,13,400/- and had incurred capital expenditure to the tune of Rs.5,73,600/- for construction of factory building between 1-1-1993 to 21-9-1994. The total assets created by the said unit were certified to be Rs.23,74,190/-. The said expenditure was certified to have been financed out of the various items stated in paragraph No.8 of the certificate, which included share

capital of Rs.5,10,000/-. The Certificate of Incorporation of M/s Maimoon Textiles Pvt. Ltd. shows that the Company was incorporated on 13th May 1993. Hence, it is evident that, as on 1-1-1993, the Company was not incorporated. Hence, the respondent could not possibly have verified the books of account for the period between 1-1-1993 till 13-5-1993. If the respondent had verified the Articles and Memorandum of Association, he would certainly have come to know that the company was incorporated on 13-5-1993, and in that case, he would not have stated that the said expenditure had been incurred between 1-1-1993 to 21-9-1994. Thus, the respondent does not appear to have verified either the Articles and Memorandum of Association or the books of accounts prior to the issuance of the certificate in question. In this context, it is also necessary to take note of the fact that the respondent tried to explain away finalization of accounts and signing of Balance Sheet as at 31st March, 1994 reflecting capital of Rs.4,000/- only by stating that share capital was raised between 31-3-1994 and 26-9-1994, the date of issuance of certificate. No evidence in this regard has been brought on record. However, even if this averment is accepted at face value, there is no explanation for alleged incurring of expenses from 1-1-1993 onwards in absence of any satisfactory source of funds established by bringing cogent evidence on record.

8.1 In the certificate, the respondent has stated that the company had raised a share capital of Rs.5,10,000/-. Upon being asked as to which documents he was required to verify for ascertaining the share capital raised by the company, the respondent had replied that one is required to verify Form No.2 and the List of Shares. However, the respondent admitted that he had not verified Form No.2, but had verified only the List of Shares.

8.2 Section 75 of the Companies Act, 1956, deals with "Return as to allotments". Sub-section (1) of Section 75 of the Companies Act, 1956 reads as under :

> "75. (1) Whenever a company having a share capital makes any allotment of its shares, the company shall, within thirty days thereafter, -
>
> (a) file with the Registrar a return of the allotments, stating the number and nominal amount of the shares comprised in the allotment, the names addresses and occupations of the allottees, and the

amount, if any, paid or due and payable on each share:

[Provided that the company shall not show in such return any shares as having been allotted for cash if cash has not actually been received in respect of such allotment;]

(b) in the case of shares (not being bonus shares) allotted as fully or partly paid-up otherwise than in cash, produce for the inspection and examination of the Registrar a contract in writing constituting the title of the allottee to the allotment together with any contract of sale, or a contract for service or other consideration in respect of which that allotment was made, such contracts being duly stamped, and filed with the Registrar copies verified in the prescribed manner of all such contracts and a return stating the number and nominal amount such contracts and a return stating the number and nominal amount of shares so allotted, the extent to which they are to be treated as paid-up, and the consideration for which they have been allotted; and

(c) file with the Registrar -

(i) in the case of bonus shares, a return stating the number and nominal amount of such shares comprised in the allotment and the names, addresses and occupations of the allottees and a copy of the resolution authorizing the issue of such shares;

(ii) in the case of issue of shares at a discount, a copy of the resolution passed by the company authorizing such issue together with a copy of the order of the Court sanctioning the issue and where the maximum rate of discount exceeds ten per cent, a copy of the order of the Central Government permitting the issue at the higher percentage.

(2) xxxxx

(3) xxxxx "

8.3 Form No.2 of Appendix I of the Companies Act, 1956 contains the particulars prescribed for filing return of allotment, as required under the provisions of Section 75 Sub-section (1) of the Companies Act. Thus, it was the primary duty of the respondent being a professional accountant to verify Form No.2 prior to certifying the share capital of the Company. Moreover, the respondent did not produce any documents in support of the fact that he had verified the List of Share Holders. The respondent was also not aware as to who were the auditors of the company. According to the annual return filed by the company with the ROC, as on 31-3-1994, the paid up capital was Rs.4,000/- and as on 31-3-1995, again the share capital was Rs.4,000/-, however, the respondent had certified the same to be Rs.5,10,000/-. The respondent has issued the Certificate in question, showing capital without such funds being available and without the capital being reflected in the books of account. The learned Senior Advocate for the petitioner Institute, is, therefore, right in contending that this is not a case of mere carelessness but a case of gross negligence, within the meaning of clause (7) of Part I of the Second Schedule to the Chartered Accountants Act, 1949.

8.4 The respondent has not produced any documentary evidence in support of his say that he was actually taken to some other site, nor is the explanation tendered by the respondent a plausible one. When as early as in February 1995, the respondent was aware of the inquiry regarding the certificate issued by him, there was no justifiable cause or reason for him to destroy the working papers. Hence, the Council was fully justified in holding that the respondent had failed to disclose material fact known to him which was not disclosed in the financial statement, but disclosure of which was necessary to make the statement not misleading, and was, therefore, guilty of professional misconduct within the meaning of Clause (5) of Part I of the Second Schedule to the Act. The Council was also justified in holding that the respondent had failed to report the material mis-statement known to him to appear in a financial statement with which he was concerned in his professional capacity and was, therefore, guilty of professional misconduct falling within the meaning of Clause (6) of Part I of the Second Schedule to the Chartered Accountants Act.

8.5 Such great faith has been reposed by GSFC upon a certificate issued by a Chartered Accountant that the same is made the basis for disbursement of funds to the loanee. The conduct of the respondent in issuing a certificate which does not state the correct facts, makes the certificate issued by a Chartered Accountant suspect, and results in lowering the esteem of the entire fraternity of professional accountants and brings disrepute to the Institute as a whole. As rightly contended by the learned Senior Advocate for the petitioner, the very purpose of obtaining a certificate is frustrated if the certificate cannot be relied upon. From an overall view of the facts, it is evident that the respondent has not exercised due care and caution in the discharge of his duties, and is guilty of being grossly negligent in the discharge of his duties and has thereby committed professional misconduct within the meaning of Clause (7) of Part I of the Second Schedule to the Chartered Accountants Act, 1949.

8.6 The respondent - delinquent has laid great emphasis on the internal control check mechanism of GSFC to seek benefit qua his own default. He has also reiterated the aspect of repayment to GSFC in this regard. However, the internal controls which are used by GSFC in its own administrative exigencies cannot deflect from the misconduct of the respondent. A professional cannot get away by pointing out defect or default of a third party. In the present case, whether the complainant - GSFC had acted in accordance with its own internal procedure or not, is besides the point. The Court is only required to consider the aspect as to whether the action of the respondent constitutes misconduct in light of the provisions of the Schedule to the Act. The overall conduct of the respondent does not inspire confidence, nor does it indicate that the respondent was not involved in the fraud that was sought to be perpetrated on GSFC. It is another matter that, before the actual scheme by which the funds were obtained from GSFC by way of loan for a non-existent project could be spirited away by some unknown persons, the facts surfaced on inspection by GSFC. It is significant to note that Shri Hanif Memon, the person who was supposed to have introduced the respondent to the Directors of M/s Maimoon Textiles, has not been produced by the respondent. In case, the respondent was inclined to establish that his conduct was above board, all that he was required to do was to produce Shri Hanif Memon to support his version. The respondent has failed to do so at his own peril.

9. This Court, in the case of Council of Institute of Chartered Accountants of India v. P.C.Parekh (supra), has observed that the High Court has been entrusted important function in context of the behaviour of the members of this noble profession in the disciplinary matters which come up before it. It has wide powers extending to removal from membership of the institute either permanently or for a specified period. It may direct the proceedings to be filed or dismiss the complaint. This enables the Court to examine the nature of misconduct alleged and the facts and circumstances brought on record in connection therewith against the delinquent. The Court observed that there is a serious responsibility on the court: a duty to itself, to the profession, and to the whole of the community to be careful not to accredit any person as worthy of the public confidence who cannot establish his right to that credential. However, when an important statutory body like the Council finds a member of the institute guilty of the misconduct and forwards the case to the High Court with its recommendation under Section 21(5) of the Act, its findings based on the material on record would ordinarily not be disturbed unless found to be unjust, unwarranted or contrary to law.

10. On the basis of the aforesaid principles, it cannot be said that the findings of the Council based on the material on record are unjust, unwarranted or contrary to law.

11. In the case of P.D.Gupta v. Ram Murti, reported in AIR 1998 SC 283, the Supreme Court has observed that Bar Council of India and State Bar Council are statutory bodies under the Act which perform varying functions under the Act and the Rules framed thereunder. Bar Council of India has laid down standards of professional conduct for the members. Code of Conduct in the circumstances can never be exhaustive. It was held that the Bar Council of India and the State Bar Councils are representative bodies of Advocates on their rolls and are charged with the responsibility of maintaining discipline amongst its members and punishing those who go astray from the path of rectitude set out for them.

12. The petitioner Council is a custodian of the interests of the profession. It is charged with the responsibility of ensuring proper conduct of the members of the Institute, to protect the interest and prestige of the profession as well as to take disciplinary action against any member who indulges in conduct which lowers

the esteem of the profession. In the present case, the petitioner Council, through its Disciplinary Committee, has considered all the relevant circumstances and has found the respondent guilty of misconduct within the meaning of Clauses (5), (6) and (7) of Part I of the Second Schedule to the Act, read with Sections 21 and 22 of the Act. We find no reason to take a different view.

13. The learned Counsel for the respondent had also laid great stress on the fact that the respondent had seen to it that the dues or the Corporation were repaid; this at best can be a mitigating factor, which could be taken into consideration while deciding on the question of quantum of punishment. However, looking to the nature of the professional misconduct committed by the respondent, no intervention is called for as regards the penalty recommended by the petitioner Council.

14. We, accordingly, uphold the finding of the Council holding the respondent guilty of misconduct within the meaning of Clauses (5), (6) and (7) of Part I of the Second Schedule to the Act, read with Sections 21 and 22 of the Act and direct that the respondent be removed forthwith from the membership of the Institute for a period of one year. The Reference stands disposed of accordingly, with no order as to costs.

[D.A.MEHTA, J.]

[H.N.DEVANI, J.]

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